THE RECOVERY FROM THE DEPRESSION

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The twelve months prior to the panic of October and November, 1907, was a period of high levels in practically every trade and industry. The steel and iron reports surpassed all records previously obtained; the country's agricultural values mounted to totals far beyond any reached before; railroad and other transportation earnings soared to wonderful heights, and in practically all retail and general distributing lines vast activity was notably the feature.

This twelve months' period and that immediately preceding it was a time of high and steadily ascending commodity prices and of high and steadily rising rates for money. The time money rates in New York and the other large centers ranged steadily above five per cent, and early in 1907 even six per cent was regarded as not excessive for the temporary uses of loanable funds. In the commercial paper market even higher rates than six per cent were considered not excessive, and all through the spring months of the year prime paper was being placed in large amounts on bases which cost the borrower anywhere from six and one-half to eight and one-half per cent, and in some instances considerably more. The loaning of money on call in the financial markets was on an equally high basis. Not only did the call money market not "loosen up," after the stringency of the fall and winter of 1906-07, but the rate steadily maintained its average above six per cent and frequently soared during the spring to new and unusual heights. It is unnecessary to say that during this period bank credits were enormously extended and reserves everywhere depleted.

The tremendously inflated level which had been reached in practically every field of industrial and commercial activity was concisely reflected by the condition of the security markets at that time. The prices of active shares on the New York Stock Exchange were hovering around figures which, in the light of dividend returns, were ridiculous in the extreme; stocks which had no

dividend-paying power whatever were in many cases selling close up to their par values; while bonds of the better type, which, in the times of easy money a year or two back had sold freely on a three and one-quarter to three and one-half per cent basis, were commanding prices which gave a yield of but four per cent or a little more, right in the face of a permanently fixed six to seven per cent money market.

Many theories have been advanced to explain the panic of 1907, and the brief period of depression which followed in its train. But as a matter of fact the causes of the panic were so patent that they have never needed explaining. The facts regarding the year preceding the panic, which I have stated in the foregoing paragraphs, are the panic's explanation. That the country was riding for a fall during this entire period is now apparent to the most superficial observer. The vanishing point must ever be reached in material activity when mounting commodity prices, climbing interest rates, distended bank credits and feverish "prosperity" are found traveling side by side.

The interesting question, however, which still begs for an intelligent answer, is an explanation of the unusual phenomena which have followed in the wake of the panic. Any careful analysis of events during the past two years will show that this period is altogether unique as compared with former depressed periods that have been outgrowths or aftermaths of panics. Just as ante-panic times are characterized universally by a rising trend in prices of commodities, in advancing wages, over-valued lands and a high level for interest rates, the few years of liquidation which logically follow are noted for a radical lowering of all commodity costs and prices, a heavy fall in wages, the bursting of all land value bubbles and the decline of interest rates to comparatively nominal levels. This was the case of the panic of 1873; it was true during the troubled years after 1893. And in other countries, where panics have occurred, these were the cardinal characteristics of the years which came after.

And in the security markets, which are each decade becoming more and more a concrete reflection of the trend of general conditions, due to the rapid absorption of all business undertakings under the corporate form, the same features have been regarded as the earmarks of after panic periods. Prices of securities, after the

temporary but extreme collapse of the panic itself, have always in the past, after their normal rebound, settled down to a basis of slow but steady liquidation which has sometimes extended over a period of a year or more. After the 1873 panic, this liquidating period was present for at least three years; after 1893 we had two periods of liquidation in the security markets, one in 1894, another in 1895 and 1896. In each case the course of the security markets directly reflected the state of trade and the general industrial situation throughout the country.

But we find that since the panic of 1907, these former normal events have apparently not taken place. We have had no real period of liquidation, either in the general industrial field or in the security markets. We have had no extended period of falling prices of commodities, nor any very pronounced price declines whatever, barring a few specific industries. While the price level reacted moderately from the high average of August, 1907, it did not drop radically, and within six months of the panic was resuming its upward trend again. At this writing, as shown by Bradstreet's, it has risen once more to about the highest average of the ante-panic year.

There has been no heavy fall in wages, such as has characterized periods following previous panics; and the wage level to-day is in many industries fully up to the plane of 1906-07, and in many instances considerably above it.

At practically no time during the past two years have wages held at the comparatively low levels following other panics; and this has been true despite the fact that when industry dropped to its lowest ebb, the labor market recorded an enormous surplusage and a larger percentage of skilled labor was out of work than had been the case for a decade before.

In the bursting of land speculation bubbles, we have always heretofore recognized a cardinal feature of after-panic periods. But this time there has been no such thing as a slump in land values. Instead, we have witnessed both urban and agricultural land retain its full value through the entire two years; inflation in prices has practically never halted, and to-day values of this nature are soaring as never before.

And if we examine the trend in the rate of interest, we will find the unusual phenomenon present here also. It is true that with

the cessation of the enormous speculative and industrial activity immediately following the panic, interest rates dropped quickly to normal figures; bank credits were liquidated in vast volume, and reserves piled up to unusual amounts. Money was a drug on the market, as it could not help but be. But while money was plentiful, it was not cheap. It is not cheap to-day. With reserves heavier than ever before in history, the trend of the money market in the financial centers has at no time been downward since 1907, and within a single year after the panic-collapse, resumed its upward trend. While for a few months it was confidently predicted in New York that the money troubles were over for another decade, and that we would soon see high-grade railroad and government bonds selling on the levels of 1902 again, this position was soon abandoned by the thoughtful. In 1902 the highest type of railroad bond, like Lake Shore first mortgage 3½'s sold on a basis to yield but three and one-eighth per cent. Many anticipated that prices would return to this level again, after the fall in money rates after the panic. But these prices have at no time been even approached, and for the last six months the trend has been quite definitely in the other direction. If we look across the water we find the same situation demonstrated. English consols once sold on a basis to yield but two per cent. This was not the result of credit, for the credit of the English nation has since risen to even greater heights; and yet to-day we find that, like the owner of Lake Shore 3½'s, the holder of British consols faces a shrinkage in principal equaling more than twenty per cent from the high figures of a few years ago.

Superficially, money seemed easy for awhile. But it has at no time been really cheap. Prior to 1906 first mortgages were easily negotiable in all the Eastern centers on a four to four and one-half per cent basis; but ever since the panic year, six per cent money in this field has been far more easily placed, and to-day is in greater demand than ever. Commercial paper has not, for even the shortest periods, settled back to the bases of former times of cheap money, and there has been immense truth in the remarks heard from merchants during the past year that "there is plenty of money, the banks tell us, but we have to reach mighty high to get any of it."

I am fully aware that comparisons with former industrial periods are dangerous things to make, and that the point will be

immediately raised that special factors can be shown to account for the long periods of liquidation after the panics of 1873 and 1893. All of which may be true, but the fact remains that whether these periods had been long or short, they would have followed as the normal outgrowth of the burst of inflation which preceded them. When the foundations are removed from under the house, the house should logically fall, even though events may quickly follow to repair the wreck and set the building up again. But although we had a panic in 1907 and the foundations were apparently removed, the house has really never fallen. We have had no real period of liquidation; no abnormal drop in wages, no slump in commodity prices, no collapse in land values, and no return in the cost of money to the levels of other normal times.

Instead of this logical sequence of events, what do we find? As a concrete reflection of other things, let us take for example, the security markets. The fall in security prices in 1907 which was occasioned by the panic conditions, aggregated a truly enormous sum. At that time I was at some pains to ascertain what this vast decline might reach in round figures, taking into consideration practically all the corporate capitalization in the country. I found that on a total par value of about thirty billions of dollars, and a market value of twenty-seven billions, there had been a shrinkage of fully ten billions of dollars within the short space of ten months. In other words, while the corporate stocks and bonds quotable in this country enjoyed a market valuation of about twenty-seven billions in January, 1907, by the middle of November of the same year this valuation had shrunken to about seventeen billions of dollars. More than one-third of all the corporate values in the United States had disappeared in ten short months like a mist before the morning sun.

But the rebound in these valuations was immediate and spontaneous. No long period of low prices ensued, as has always hitherto been the case after a financial cataclysm, and it is entirely true that the "bull market" in active securities has continued without any important break from November, 1907, to the present date. To-day the security valuations as a whole are back to the levels of 1906 again, with this difference, they do not seem to be on the brink of a precipice, but rather only part way up the hill toward a distant summit.

This remarkable and uninterrupted rise in security valuations definitely reflects the trend in all fields of commercial effort. Industry has awakened in nearly every line, all trades are taking the optimistic view that they are entering upon a period of unusual activity. But the following difference must be noted between the two years' record of security quotations and the activity of business itself. While stock valuations have been steadily growing, business activity remained at a low ebb until within the past eight or ten months. The revival in production assumed its logical sequence as after other panics. It did not begin until a reasonable period of intense dullness had preceded it.

But just here is where the unusual situation comes in. After previous panics, the revival has never taken place except upon a level of low prices for commodities and a considerably lower wage scale, accompanied by the cessation of extensive liquidation of inflated land and other artificial values. In other words, the present period of business activity and advancing prices has started from its approximate high level of the ante-panic year and we are building upward from the roof instead of starting from the ground.

The thoughtful student can only regard this entire situation as unusual and unique. It cannot, in my opinion, be explained away in any touch-and-go fashion. There must be some underlying cause at work of more than ordinary nature to account for a situation which is absolutely new in economic history.

It is not merely the "spirit of speculation" which so thoroughly permeates the American people. This is not the cause; but it is one of the earmarks of the true cause. Let us probe a little deeper. Rising prices, rising interest rates, growing profits, stationary or moderately rising wages, increasing costs in every line, expanding values of realty and of legal benefits; they can all be traced largely to one general cause. This cause is not the "awakening of prosperity." We had all this phenomena present when prosperity was asleep; stock prices climbed steadily up while industry slept; commodity prices nearly maintained their levels or increased when the markets were glutted; realty values soared when they ought to have come down; money commanded its price when bank reserves overflowed.

Now either values are actually rising or the thing by which we measure them in shortening. I believe the latter to be the case.

The decreasing value of gold, due to its enormous production, is steadily depreciating the value of our money standard, and having an effect of far-reaching nature on our whole industrial fabric. Probably it is safe to say that the value of the gold dollar, in relation to other things, has declined to the extent of at least forty per cent during the past eight or ten years, and the trend is still in the same direction. This it is which has caused the unusual stability in commodity prices during the past two years; it has largely accounted for the maintenance of high valuations for real estate and steadily increasing costs in every line. It has tended to maintain interest rates at a higher level than was formerly normal, and is largely back of the remarkable advances in stock market valuations which we have witnessed ever since the close of 1907. For let it not be forgotten that the great rise in security values is found chiefly among the stock issues of unlimited dividend paying power, and not among high grade mortgages of limited income. The latter, in response to the prevailing strength of the money market, have never returned to the bases which they enjoyed a few years ago.

I believe that the banker, business man, student or ordinary observer who fails to give proper attention to this phenomenon, and undertakes to forecast coming events in business and finance without considering its effect, will be in danger of going far wrong in his calculations. We have not, in my opinion, entered a long period of prosperity similar to that which obtained from 1898 to 1907; we are not justified in expecting another ten or twenty years to pass before we have to face a recurrence of business disaster and panic. In fact, I do not believe we are justified in expecting, unless new signs appear on the horizon, a period of more than two or three years more before we will be in danger of facing a crisis far more serious and far-reaching in its effects than that of two years ago.

For if advancing prices and abnormally rising values mean anything, they mean speculation. They nurse the speculative desire as nothing else can; they divert effort from normal to abnormal channels. The "holding for a rise" is as potent an element of speculation in the dealings between merchants and their customers and between manufacturers and their buyers, as it is in the purchasing of wheat, cotton, stocks or real estate. And the more steady and intense the rise in prices, the more rapidly the fever of

speculation spreads, until, as is inevitable as long as consumption has its limit, the unavoidable crash arrives.

Barring this far-reaching factor, I think the present revival from the panic is healthy and sound. I do not think we stand in danger of any immediate set-back in industrial activity or in commercial fields as a whole. Rather I believe we may look forward to a continuance of rising prices for many months to come, increased railroad earnings with perhaps smaller profits relatively, due to the limitation of rates, phenomenal profits in some of the industrial fields and an unusual volume of business in most retail lines. But I also believe that we will witness a continuance of the upward trend in commodity prices, further high valuations for realty, advancing and higher interest rates; phenomena which in time must work the undoing of this peaceful period, and cause us to press for solution a factor which is robbing us of our future safety almost without our knowing it.